

Dilemma: doing business with a distributor or an agent?

A common dilemma faced by many Italian suppliers and manufacturers is how to develop connections with UK commercial partners in order to break into the UK market.

The unparalleled richness and diversity of Italian products, known overseas as the “Made in Italy” effect, corresponds well with the Italian sense of individuality, quality and anti-global culture.

Although “Made in Italy” products may appear more competitive than others in overseas markets, the success of a product depends on a combination of legal and commercial factors which need to be considered before launching a product outside the domestic market.

Naturally the safest and most prudent route before launching a product into a new market is to seek advice from a lawyer qualified to act in the relevant jurisdiction.

Suppliers and manufacturers may decide to focus on marketing and selling their products through an agent or distributor in a cost-effective manner that maximises profit while promoting and increasing demand within an overseas market.

An Italian supplier or manufacturer (known for contractual purposes as the principal) can engage a UK agent to undertake a variety of business activities. A typical agency relationship arises where the UK agent contracts on behalf of its principal to market and arrange sales of products to UK customers while receiving a fixed or variable commission. The agent thus establishes a direct contractual relationship between the principal and the UK customer without taking on any contractual liability itself towards the customers.

A UK distributorship arrangement may be used where a distributor purchases goods from an Italian supplier or manufacturer for resale to his/her UK customers. The distributor makes a profit from the margin as added on the resale of such products and passes title to the products to the customers directly. The distributor takes on contractual liability for the sale of the products and no relationship is formed between the supplier/manufacturer and the UK customer.

The first step for any Italian supplier or manufacturer considering launching a product into the UK market should be whether an agency or distributorship arrangement would suit their business model. The crucial element is to find an agent or distributor that will undertake and develop the UK business in accordance with the Italian supplier/manufacturer’s business requirements and needs.

Looking more closely at the differences between these two forms of business it is clear that each has its advantages and disadvantages.

Employing an agent means that the Italian supplier/manufacturer retains greater control over how the product is marketed, sold and what after-sale service is offered. It is easier for the Italian company to retain control over the agent’s activities and monitor the success of the product launch. Furthermore the Italian company can benefit from the agent’s knowledge of the local trading conditions and take advantage of the customer contacts that have already been developed by the agent.

The main disadvantage is of course that when employing an agent, it is the Italian manufacturer/supplier that will retain all legal and commercial risks, for instance, in respect of product liability, disputes and in many cases a statutory obligation under the Commercial Agents Directive to pay compensation to the agent on termination.

In case of a distributorship arrangement, here the main benefit is that once the product is sold to the distributor, the Italian supplier/manufacturer has no contractual responsibility for the costs and commercial risks with respect to the development of the distribution business in the UK, although it will of course still be concerned to ensure that its product is properly marketed and sold by the distributor. The Italian company can then concentrate on product development and targeting new markets.

The main disadvantage of a distributorship arrangement is the lack of connection between the UK end-user/customer and the Italian supplier/manufacturer. It is therefore more difficult for the Italian manufacturer to monitor trends in the UK market which naturally effect product development. In the same way, the supplier may have to accept having less control over the distributor's marketing techniques or pricing policy.

One of the main reasons for obtaining good legal advice is not only to ensure compliance with the local legislation in the foreign market, but also to determine how terms of an agreement may be challenged or affected by EU competition law which has an increasing role to play in respect of cross border relationships.

Although under English law an agency or distribution agreement can be made verbally, this is not recommended and generally leads to problems and disputes later on. It is always better to set out agreements in writing so each party is clear as to own rights and obligations.

Before commencing business, the parties should ensure that any relevant third party's consent and/or local approvals are obtained and that express provisions in the agreement deal with the key issues, including intellectual property rights, term, notice period and compensation.

Consideration should also be given in respect of the tax position. A key area to consider is whether or not by employing an agent or distributor the Italian supplier/manufacturer would be deemed to have a permanent establishment in the UK. This may be relevant for tax purposes in order to establish whether or not the Italian supplier/manufacturer would be subject to the double-taxation regulations.

"Made in Italy" is certainly an ongoing success story in its own right. However, for Italian manufacturers and suppliers to tap into this success and market their products to overseas customers, prudent step by step planning is essential. Specialist legal advice in the overseas country is crucial to any successful product launch and development.

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Note: *These articles are not intended to be a complete guide to the law to which they refer. Specific problems should be referred to a member of the firm before any action is taken.*